Estate Taxes

Practitioners Express Mixed Reaction To Valuation Discount Legislation

A new bill to nullify proposed regulations aimed at curbing valuation discounts is getting mixed reviews, but practitioners in the estate planning industry said it could set the tone for an upcoming debate on the rules’ legitimacy.

The bill, H.R. 6042, introduced by Rep. Jim Sensenbrenner (R-Wis.) on Sept. 15 calls for the revocation of regulations the Internal Revenue Service proposed in August.

The rules (REG-163113-02) place limitations on the use of valuation discounts that reduce the overall value of assets held in family-owned businesses, thus lowering estate and gift tax liability. They are typically applied to compensate for the lack of marketability and control that can make assets within those entities harder to sell (149 DTR G-4, 8/3/16).

In a news release, Sensenbrenner said his bill would nullify the IRS regulations, which would make it “difficult for family-owned businesses to keep their doors open.” The bill proposes that the rules and “any substantially similar regulations hereafter promulgated, shall have no force or effect.”

When asked why the legislation was introduced before waiting to see what the IRS includes in the final regulations, Nicole Tieman, the congressman’s communications director, said: “Because more than half of the economy is supported by small and family-owned businesses. That’s millions of people this bill can potentially help.”

Tieman called the IRS proposal “an attempt to sidestep Congressional oversight” in a Sept. 16 e-mail to Bloomberg BNA.

A spokeswoman for the House Ways and Means Committee said: “Chairman Brady also has strong concerns about these regulations and appreciates Congressmen Sensenbrenner’s leadership on this issue.”

The chairman is reviewing the bill and “continues to focus on fully repealing the death tax through our tax reform blueprint,” she said in an e-mail to Bloomberg BNA.

While several practitioners and associations that represent family businesses also lauded Sensenbrenner’s efforts, at least one attorney said he sees the bill as “unnecessary.”

‘Overreaction.’ The legislation is an “overreaction to the proposed regulations,” Ron Aucutt, a partner at McGuireWoods LLP, told Bloomberg BNA on Sept. 16.

Whatever issues there are with the proposed regulations should be fixed in the normal regulatory process of making comments and participating in the Dec. 1 IRS hearing, he said. “I think the IRS is open to those kinds of suggestions,” he said.

Aucutt said the government should abide by its own laws and practices. “I think that Congress delegated very clearly in 1990 the authority for the IRS to publish these regulations and that should be the end of it.” If Congress believes the regulations aren’t a valid exercise of the agency’s authority, lawmakers can change the statute and take that authority away, he said.

“I don’t think that it’s a very good model to have this kind of congressional or legislative intervention in a regulations process that’s being done under an authority that Congress granted, unless there’s some really drastic abuse, and here I don’t see it,” Aucutt said.

Attention Grabber. Scott Ditman, a certified public accountant and tax partner at Berdon LLP, said while he agrees the regulations should “play out in the normal setting,” he’s very pleased with the bill because “it will draw attention to the real negatives in the proposed regulations.”

When the valuation discount rules first came out, Mark Mazur, assistant secretary for tax policy at the Treasury Department, said the guidance would “close a tax loophole that certain taxpayers have long used to understate the fair market value of their assets for estate and gift tax purposes.”

Ditman said he understands the IRS’s desire to crack down on abusive transactions where wealthy families have applied valuation discounts to partnerships containing marketable securities such as stocks and bonds that could be easily valued and sold. However, the rules were written so broadly that they “attacked pretty much every transfer of any kind of a business inside of an entity,” he said. That means that not only would a cash or marketable security partnership be affected, but also a legitimate operating business, he said.

Those businesses were taking valid discounts and now “I could die and all of a sudden my estate taxes could be so much more than they would have been,” he said. “And if I didn’t plan for it or I have no exit strategy, my family could be forced to sell a real business, whether it’s real estate, a farm or an auto dealership,” he said.

Ditman said the bill could assist in efforts to get the regulations withdrawn or revised “because if people really see what’s going on, maybe the hearings will be more heightened and maybe the IRS will pay more attention to it, because they’ll see that the negative reaction is broad-based.”
Associations React. While not having had a chance to review the bill himself, Matthew Turkstra, manager of legislative affairs for the National Federation of Independent Business, said he disagrees with the IRS’s proposed regulations.

“NFIB is working with our coalition partners in the Family Business Estate Tax Coalition (FBETC), to see these misguided regulations are withdrawn,” Turkstra told Bloomberg BNA in an e-mail.

“As proposed, they would make it harder for family-owned enterprises to survive from one generation to the next, divert capital from business investment and cost jobs,” he said.

Edward Tarlow, president of the Family Business Association Inc., said he supports Sensenbrenner’s bill. Family businesses already face the burden of regulations and compliance, Tarlow told Bloomberg BNA Sept. 16.

“Eighty percent of new employment comes from small businesses and 80 percent of those small businesses are family businesses,” and “if they’re going to make it more difficult to pass businesses on to the next generation by imposing taxes” they will eliminate the mechanism that does much of the hiring, he said.

“All you’re doing is forcing the smaller businesses out of existence and you’re creating some kind of middle market,” Tarlow said.

Delay, Delay, Delay. Another reason practitioners are applauding the congressman’s efforts is because any negative attention to the regulations in their current form could cause a delay to the effective date.

According to wealth planners, the Obama administration has said it would like to have the valuation discount rules finalized before the current president leaves office, which means the guidance could be effective as early as January (171 DTR G-4, 9/2/16).

“Quite frankly, anything that either delays these regulations being passed in their current form or gets them revised to be fair to the families that really need those valuation discounts is a good thing,” said Lori Anne Douglass, a partner in the Trusts and Estates Group at Moses & Singer LLP.

To the extent that families have more time to do estate planning before the rules become effective, “delay is a good thing,” Douglass told Bloomberg BNA.

Not Going Anywhere. All three practitioners said the bill on its own is unlikely to go anywhere.

“There are a lot of legitimate uses of congressional energy that there isn’t enough time to do this year anyway, and this is just a distraction that I expect to go away,” Aucutt said.

The bill probably won’t pass Congress but will play an important role in the overall conversation that occurs to have the regulations either withdrawn or revised, Douglass said.

Ditman agreed. He welcomed the attention the bill will bring to the rules, but said the legislation “is not going to have any legs on its own.”

Aucutt noted that the legislation is sure to be a hit with constituents. “I have no doubt that there are a lot of constituents that are quite worked up about this,” he said. “There are a lot more bills introduced than passed, of course, and this is a way to respond to constituents,” he said.

The bill’s message is “consistent with a narrative—that a lot of people subscribe to—that the Obama administration is inclined to do things by regulation in defiance of congressional intent or prerogative.”

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Text of H.R. 6042 is in TaxCore.